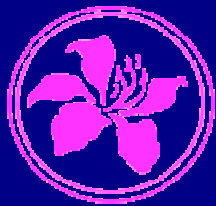


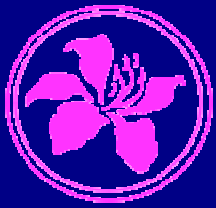
Hong Kong Banking Sector: 2010 Year-end Review and Priorities for 2011

Hong Kong Monetary Authority
27 January 2011



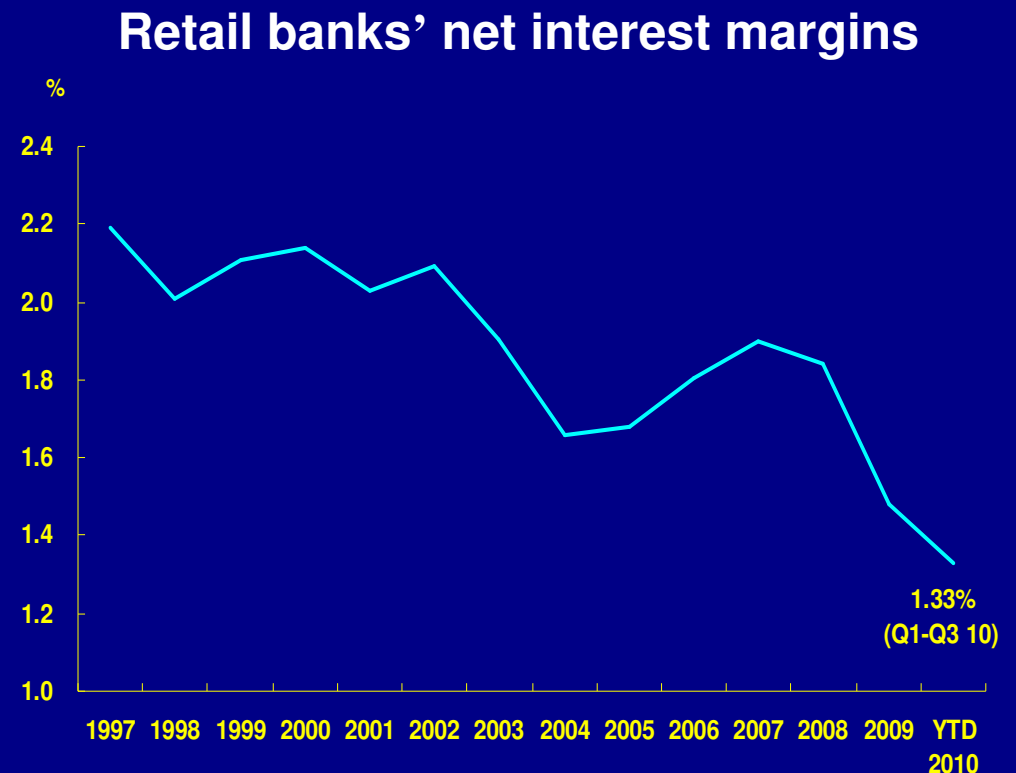
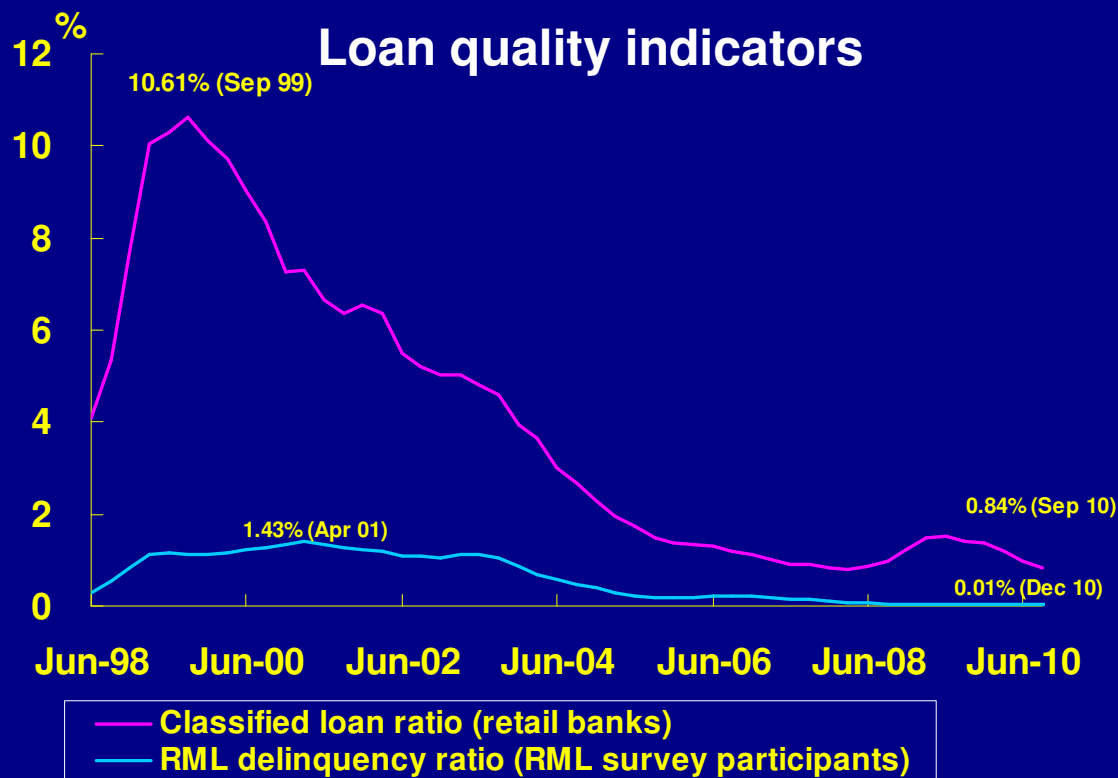
Performance of the banking sector (1)

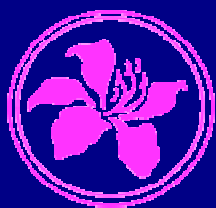
- The pace of global economic recovery was uneven
- The banking sector in Hong Kong remained resilient despite uncertainties in the global landscape
- Profitability increased but net interest margins remained under pressure
- Improved asset quality and sound capital / liquidity positions



Performance of the banking sector (2)

- **Loan quality continued to improve**
- **Net interest margins at historically low levels**

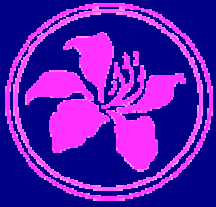




Performance of the banking sector (3)

Other Indicators	<u>2010</u>	<u>2009</u>
• Total loans	+28.6%	+0.1%
• Residential mortgage loans	+15.1%	+9.0%
• Non-bank China exposures	+41.6% (first 3Q)	+17.9%
• Total deposits	+ 7.5%	+5.3%
• Loan-to-deposit (L/D) ratio	61.6%	51.5%
• HK\$ L/D ratio	78.1%	71.2%
• CAR (locally incorporated AIs)	16.1% (Sep)	16.8%

Note: Figures relate to all AIs unless otherwise stated



Key issues in 2011

Risk from mortgage loan portfolio

- Prudential supervision and positive mortgage data sharing

Loan growth

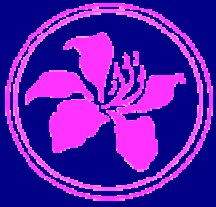
- Underwriting standards
- Loan use surveillance
- Provisioning

Basel III implementation

- International discussions
- Local legislative work

Enforcement and consumer issues

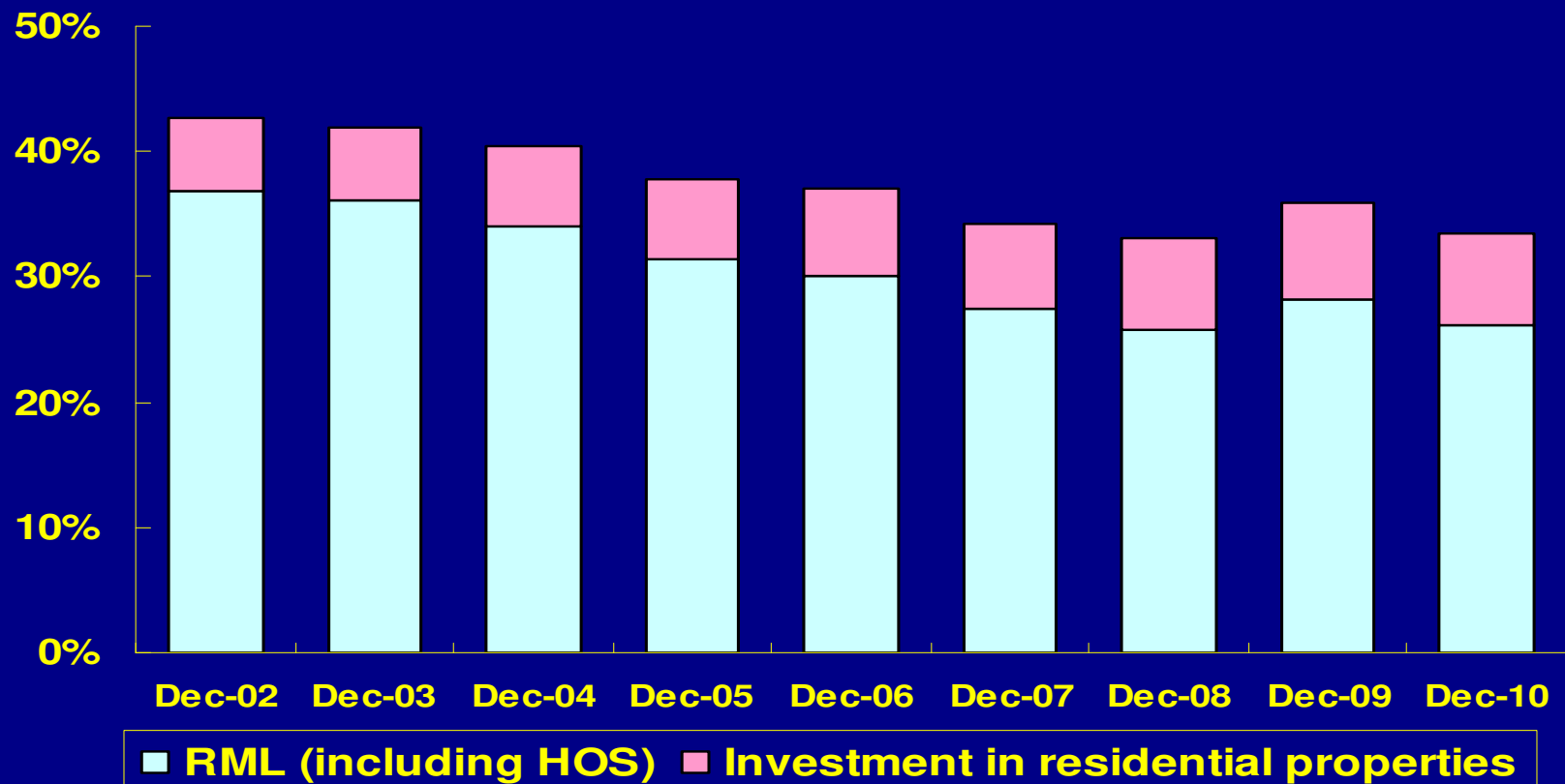
- Clear backlog investigation cases
- Consumer and investor protection, e.g. credit card reform proposal

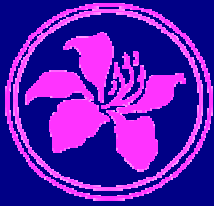


Banking Supervision (1)

- Residential mortgage loans – a long standing supervisory focus given its significance to banks' loan portfolios

as % of loans
for use in HK

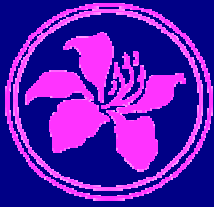




Banking Supervision (2)

For 2010

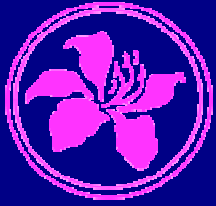
- **Prudential supervision of Residential Mortgage Loans (RMLs)**
 - Introduced prudential measures to strengthen risk management
- **Closely monitored credit growth**
 - Understood better the drivers for rapid credit growth and how to strengthen banks' credit risk management
- **Enhanced supervision of Systemically Important Financial Institutions (SIFIs)**
 - Actively participated in FSB/BCBS discussions on initiatives to enhance the regulation of SIFIs
- **Closely monitored major developments in the financial markets in the US and Europe**



Banking Supervision (3)

Supervisory focus for 2011

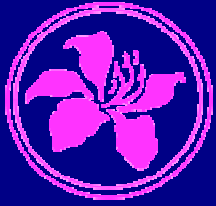
- **Step up onsite examinations of local banks' Mainland China operations and enhance communication with China Banking Regulatory Commission**
- **Thematic examinations**
 - **RML Business**
 - **Credit Growth : underwriting standards and loans use surveillance**
 - **RMB Business**
 - **Sound Remuneration System Guideline**
- **Review provisioning level against a macroprudential perspective**
- **Monitor banks' preparations for introduction of Basel III framework**
- **Continue participation in international discussions on implementation of Basel III recommendations and supervision of SIFIs**



Banking Policy (1)

For 2010

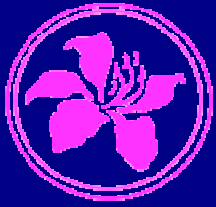
- **Proposed legislative amendments for Basel II enhancements**
- **Active participation in the international development of Basel III and other regulatory reforms**
- **Updating of Supervisory Policy Manual (liquidity risk management, remuneration, fair valuation practices and employee competence)**
- **Enhanced macro-prudential surveillance**



Banking Policy (2)

Priorities for 2011

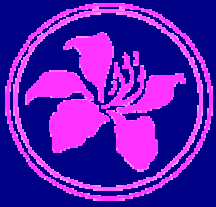
- **Preparation for Basel III implementation**
 - Industry consultation
 - Legislative amendments
 - Transitional arrangements
- **Implementation of OTC derivatives market reform**
- **Updating of Supervisory Policy Manual (corporate governance, credit risk transfer and stress testing)**
- **Further work on macro-prudential surveillance**



Banking Conduct (1)

For 2010

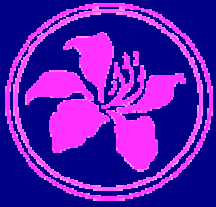
- **Focused on consumer protection issues**
 - **Enhanced instalment payment plans**
 - **Facilitated consultation on positive mortgage data sharing**
 - **Promoted review of credit card practices**
 - **Followed up on data privacy issues raised by the Octopus incident**
- **Strengthened investor protection measures**
 - **PICOP**
 - **Mystery shopping programme, etc.**
- **Enhanced DPS**



Banking Conduct (2)

Priorities for 2011

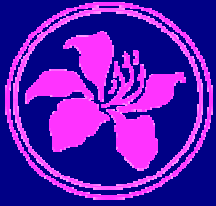
- **Consumer issues**
 - **Prepare for implementation of positive mortgage data sharing**
 - **Implement applicable credit card reform measures as soon as practicable**
 - **Enhance efforts in consumer protection, e.g. mystery shopping programme, on-site examinations of Als' compliance with Code of Banking Practice**



Banking Conduct (3)

Priorities for 2011

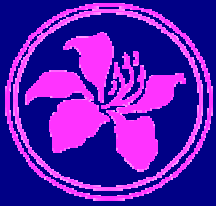
- **Investor protection**
 - Enhance selling practices for ILAS
 - Increase manpower and step up on-site examinations of sales of investment products and insurance products
 - Enhance disclosure for currency-linked and interest rate-linked investment products
 - Mystery shopping focusing on sale of unlisted investment products and insurance products
- **Implementation of enhanced DPS**



Enforcement (1)

Up to end-2010

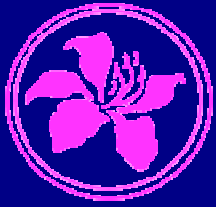
- **Investigation and follow-up work**
 - **Over 300 investigation staff employed in the peak period**
 - **About 32,600 telephone / face-to-face interviews conducted**
 - **About 290,000 pages of information / interview statements collected**
 - **About 3,200 man-hour spent by senior management staff on**
 - **104 Event Review Committee meetings**
 - **69 Disciplinary Committee meetings**
 - **About 26,400 man-hour spent on handling follow-up work arising from enforcement process**



Enforcement (2)

For 2010

- As of 20 Jan 2011, the investigation of over 99% of 21,744 Lehman-related complaint cases received has been completed. These include:
 - 2,680 cases which were closed because insufficient prima facie evidence of misconduct was found after assessment or no sufficient grounds and evidence were found after investigation
 - 506 cases which are going through the internal review process
 - 18,469 cases which warranted further action, including 16,927 cases resolved
 - 1,540 cases still under disciplinary process and 2 cases with disciplinary sanctions imposed



Enforcement (3)

Priorities for 2011

- **Continue the disciplinary process arising from Lehman-related complaints**
- **Accelerate the investigation of non-Lehman-related complaints**
- **Enhance the complaint handling and investigation process**
- **Gradually rationalise the staff resources to normal mode**